

1 contribution/profit recovered by the rate.<sup>34</sup> The underlying *cost*-basis should be  
2 the same, whether the element is required by section 251 or 271. The TELRIC  
3 pricing standard establishes the rate for a network element at its forward-looking,  
4 average cost.<sup>35</sup> Because a competitive market should produce network element  
5 prices based on marginal or incremental costs (as opposed to average total costs),  
6 comparing margins calculated using TELRIC already include contribution and  
7 provide a return. Moreover, by maintaining the same cost-basis, the Authority  
8 can focus its review on whether the additional profit sought by BellSouth is just  
9 and reasonable.

10  
11 As to the second broad category of information, BellSouth should be required to  
12 demonstrate that its proposed prices are consistent with the pricing of alternatives.  
13 Necessary information would include a listing of the specific competitors that  
14 BellSouth claims offer a wholesale alternative to its unbundled local switching (or  
15 whatever element it seeks to impose non-UNE prices upon), as well as the prices  
16 charged by those competitors.

<sup>34</sup> I do not intend to provoke a debate about whether the margin (about cost) in a particular proposed price is "profit" or "contribution" to BellSouth's joint and common costs. Whatever BellSouth feels most comfortable *calling* that margin, the important point is that information be *available* for review.

<sup>35</sup> The "TELRIC" abbreviation is something of a misnomer. Although the label implies an "incremental" costing methodology, its assignment of joint and common costs necessary to operate and manage a "network element company" effectively means that the cost standard is the average total cost of offering network elements.

**Direct Testimony of Joseph Gillan  
On Behalf of ITC^DeltaCom  
Docket No. 03-00119**

1 Another benchmark to determine the reasonableness of a BellSouth proposed rate  
2 would be to compare the retail-to-wholesale rate relationship sought by BellSouth  
3 to the retail-to-wholesale price relationship in a part of the market where  
4 competitive forces do produce “market rates.” Specifically, the Authority should  
5 review the retail-to-wholesale relationship of BellSouth’s long distance services.  
6 To provide long distance service, BellSouth leases a combination of “wholesale  
7 long distance network elements.” This comparison of retail-to-wholesale long  
8 distance prices would provide a useful context to judge the relationship between  
9 retail-to-wholesale UNE prices in the local market.

10

11 **Q. Does this conclude your direct testimony?**

12

13 **A. Yes.**



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\*Prices may vary depending upon zone. Prices do not include taxes or surcharges which will total approximately \$13 to \$14

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*Beesouth of  
19344-22  
2/21/06*

**UNE-P/DS0 W/FEATURES**

	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>E</b>
	BellSouth Proposed/Filed Cost (Dec. 2001) <sup>1</sup>	GPSC Staff Proposed TELRIC (2/2/06)	Enterprise DSO Platform (Comm. Agmt.)	MOMENTUMBiz 60	MOMENTUMBiz 600
<b>Loop (Zone 1)</b>	\$13.92	\$10.98	\$10.98		
<b>Port</b>	\$1.15	\$0.92	\$10.92		
<b>Estimated Usage</b>	\$3.16	\$2.55	\$2.55		
<b>Features</b>	\$2.27	\$0.77	\$0.77		
<b>Total</b>	<b>\$20.50</b>	<b>\$15.22</b>	<b>\$25.22</b>	<b>\$27.95</b>	<b>\$37.95</b>
<b>Vs. BellSouth Proposed Cost (Col. A)</b>			23%	36%	85%
<b>Vs. GPSC Proposed TELRIC (Col. B)</b>			66%	84%	149%

<sup>1</sup> Basis of Mr. Gillan's 271 rate. See Testimony, at 21.

*BellSouth*  
19341-5

BEFORE THE  
GEORGIA PUBLIC SERVICE COMMISSION

RECEIVED

FEB 23 2006

In Re: )  
Generic Proceeding to Examine Issues )  
Related to BellSouth's Obligations to )  
Provide Unbundled Network Elements )

Docket No. 19341-U

EXECUTIVE SECRETARY  
G.P.S.C.

ITC^DELTA COM COMMUNICATIONS, INC.'S RESPONSE TO  
BELLSOUTH TELECOMMUNICATIONS, INC.'S  
FIRST SET OF DISCOVERY REQUESTS

INTERROGATORIES

1. Provide the publicly available rate you offered for a 1FR plus 3 vertical features (or analogous package) prior to executing a commercial agreement and/or a 271 agreement with BellSouth.

RESPONSE: ITC^DeltaCom provided local residential service through its Infinity Service and its GrapeVine Service to residential customers. The majority of ITC^DeltaCom's residential customers were provided service via GrapeVine products that set a package price for local, long distance and certain vertical features. Although ITC^DeltaCom signed its Commercial Agreement with BellSouth in April 2005, it began implementing changes in its rates and/or discounts as early as March 2005 during the negotiations phase for the Commercial Agreement. In November 2005, ITC^Deltacom discontinued offering GrapeVine Service to residential customers. Please see Attachment A for additional information.

2. Provide the publicly available rate you offered for a 1FR plus 3 vertical features (or analogous package) after executing a commercial agreement and/or a 271 agreement with BellSouth.

RESPONSE: See response for Interrogatory No. 1.

Comp South of  
19341-U  
2/21/06

ATTACHMENT A

ITC^DELTACOM RESIDENTIAL LOCAL SERVICE

PRODUCT	DATE	PRIMARY LINE RATE	FEATURES INCLUDED WITHOUT CHARGE	OPTIONAL FEATURES/RATES
State of Grape (included local and long distance)	1/05	\$34.99	Call Waiting Call Waiting ID Caller ID 3-Way Calling Anonymous Call Rejection Blocking for Caller ID 900/976 Call Block International Call Block Collect Call Block 3 <sup>rd</sup> Party Block 3 <sup>rd</sup> Party Collect Call Block Toll Call Block	VM/Stutter Tone w/Call Forward Busy & Call Forward Don't Answer \$5.95 Call Forward Variable \$4.00 Call Return \$4.00 Repeat Dial \$4.00 RightRing I \$5.00 RightRing II \$7.00
	3/05	\$39.99	Same as above plus Call Return	VM/Stutter Tone w/Call Forward Busy & Call Forward Don't Answer \$5.95 Call Forward Variable \$4.00 Repeat Dial \$4.00 RightRing I \$5.00 RightRing II \$7.00
	7/05	\$49.99	Same as above	Same as above
	11/05	ITC^DeltaCom withdrew all GrapeVine products from its tariff	N/A	N/A

## Basic Methodology

*Direct Cost + Reasonable Contribution to Common/Overhead Costs*

### Direct Costs

- \* Uses *BellSouth's* Estimate of Forward Looking Costs, thereby eliminating any issue as to whether inputs are appropriate for BellSouth network.
- \* Adopts *BellSouth's* Claimed Cost of Capital of 11.25% (increase of 15%)

### Contribution to Common/Overhead Costs

- \* Applies a 20% Contribution Factor, approximately 1/3<sup>rd</sup> more than that used by BellSouth in its cost studies.

**The Result: *Higher* Prices with *Higher* Contribution and *Higher* Profits  
than §251 Elements**

*Comptroller S*  
19341-2  
2/2/06

## Proposed Just and Reasonable §271 Rates for High Capacity Loops

Loop Network Elements	TELRIC §251 Rates	CompSouth §271 Rates	Increase
<b>Local Loops</b>			
4-Wire DS1 Digital Loop - Zone 1	\$49.41	\$85.97	74%
4-Wire DS1 Digital Loop - Zone 2	\$52.55	\$81.27	55%
4-Wire DS1 Digital Loop - Zone 3	\$68.40	\$128.28	88%
High Capacity DS3 Loop – Facility Termination	\$258.44	\$323.53	25%
High Capacity DS3 Loop - Per Mile	\$11.40	\$13.47	18%
<b>Multiplexing</b>			
Channelization - Channel System DS3 to DS1	\$124.39	\$157.48	27%
Interface Unit - Interface DS3 to DS1	\$7.50	\$9.50	27%

## Local Switching

- \* **CompSouth proposes a flat-rate for local switching, recognizing that the cost structure for a modern digital switch is not usage sensitive.**

**Comparison of CompSouth §271 GA Rate to Other States/FCC**

State	Cost Measure	Rate	Proposed §271 Rate	% Above Comparable
Georgia	Average TELRIC	\$4.18	\$6.86	65%
Illinois	TELRIC	\$2.18	\$6.86	215%
Indiana	TELRIC	\$2.98	\$6.86	130%
Wisconsin	TELRIC	\$2.83	\$6.86	142%
Utah	TELRIC	\$3.55	\$6.86	93%
Minnesota	TELRIC	\$3.12	\$6.86	120%
Virginia (FCC)	TELRIC	\$2.83	\$6.86	142%
Tennessee	Just and Reasonable	\$5.08	\$6.86	35%



D



## **COMPSOUTH POST-HEARING BRIEF**

COME NOW, Competitive Carriers of the South, Inc. (“CompSouth”), on behalf of its membership,<sup>1</sup> and submit the following Post-Hearing Brief in the above-referenced proceeding.

### **I. INTRODUCTION**

The purpose of this phase of Docket 19341-U was clearly articulated by the Commission in its January 20, 2006 “Order Initiating Hearings To Set A Just And Reasonable Rate Under Section 271.” The Commission’s Order provided as follows:

[T]he Commission concludes that it is reasonable to assert jurisdiction to set just and reasonable rates for de-listed UNEs pursuant to Section 271 of the Federal Telecom Act. Pursuant to this jurisdiction, the Commission will proceed with an expedited hearing schedule as detailed below for the purpose of setting just and reasonable rates for de-listed UNEs pursuant to Section 271.<sup>2</sup>

BellSouth Telecommunications, Inc. (“BellSouth”) actively participated in this phase of the proceeding. BellSouth engaged in discovery, issuing written interrogatories to various Georgia competitive local exchange carriers (“CLECs”), as well as filing objections to CompSouth’s discovery requests. BellSouth filed testimony prepared by Dr. William E. Taylor, an economic consultant who has appeared in numerous telecommunications rate-setting proceedings. Therefore, while BellSouth has continued to vehemently object to the Commission’s jurisdiction to set just and reasonable rates under Section 271, there can be no doubt that BellSouth had every opportunity to present facts supporting its just and reasonable rate proposals for de-listed UNEs.

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<sup>1</sup> CompSouth’s members include the following companies participating in this proceeding: Access Point Inc., Cbeyond Communications, LLC, Cinergy Communications Company, Dialog Telecommunications, DIECA Communications, Inc., d/b/a Covad Communications Company, FDN Communications, IDS Telcom, LLC, InLine, ITC^DeltaCom, LecStar Telecom, Inc., Momentum Telecom, Inc., Navigator Telecommunications, LLC, NuVox Communications, Inc, Supra Telecom, Talk America (and Network Telephone, a Talk America company), Trinsic Communications, Inc., XO Communications Services, Inc., and Xspedius Communications, LLC.

<sup>2</sup> Docket 19341-U, Order Initiating Hearings To Set A Just And Reasonable Rate Under Section 271, at 4 (Jan. 20, 2006) (“Order Initiating Hearings”).

Similarly, there can be no doubt that BellSouth actively used those opportunities by sponsoring testimony and extensively cross-examining CompSouth's witness at hearing.

At the end of the hearing, however, it was clear that BellSouth failed to put forth evidence supporting rates meeting the just and reasonable standard under Section 271. BellSouth pointed to its "commercial agreements" for unbundled switching and its tariffed special access rates for high-capacity loop and interoffice transport, but it did not identify exactly what those rates are or why the particular rates (or range of rates) proposed meet, as the FCC required, the "basic just, reasonable, and nondiscriminatory rate standard of [Communications Act] sections 201 and 202 that is fundamental to common carrier regulation that has historically been applied under most federal and state statutes, including (for interstate services) the Communications Act."<sup>3</sup>

By contrast, CompSouth provided specific rate proposals that satisfy the Section 271 just and reasonable standard. CompSouth's proposals are based on the application of rate-setting principles that even BellSouth's witness admitted are sound and practical. CompSouth's proposed rates for de-listed high-capacity loops, transport, and switching are significantly above the TELRIC-based rate levels that apply to UNEs remain available under Section 251 of the federal Act. At the same time, the CompSouth's proposal would establish rates that still give competitors a meaningful opportunity to compete in the Georgia local market.

Neither the federal Act nor the FCC's interpretations of it excuse BellSouth from continuing to meet its obligations under Section 271. Those obligations apply only to former Bell Operating Companies ("BOCs"), and reflect Congress' concern that after long-distance

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<sup>3</sup> Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deployment of Wireline Services Offering Advanced Telecommunications Capability, CC Docket Nos. 01-338, 96-98, 98-147 Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, 18 FCC Rcd 16978 (2003) ("TRO") ¶ 663.

entry the BOCs must live up to obligations that do not apply to all incumbent local exchange carriers (“ILECs”). Due to their historic position and market power, the BOCs are in a unique position to hinder local competition, and Congress incorporated the Section 271 checklist to prevent such market power from being exercised. BellSouth’s position on its Section 271 rate obligations would drain Section 271 of any meaning by permitting BellSouth to operate as if Section 271 unbundling obligations did not exist. In BellSouth’s view, Section 271 standards should not prevent BellSouth from doing what it would have done if Section 271 did not exist; namely, driving all wholesale customers of its high-capacity loop and interoffice transport facilities to exorbitant tariffed special access rates, and offering wholesale switching only subject to commercial agreements priced as BellSouth sees fit. That outcome is not what the Congress or the FCC contemplated in the statute or in the TRO and TRRO.<sup>4</sup>

CompSouth’s rate proposals meet the just and reasonable standard and should be adopted by the Commission.<sup>5</sup>

## **II. THE COMPSOUTH AND BELL SOUTH RATE PROPOSALS**

### **A. Overview.**

CompSouth’s proposed just and reasonable rates for de-listed high-capacity loops, interoffice transport, and switching were included in the pre-filed testimony of Mr. Joseph

---

<sup>4</sup> In the Matter of Unbundled Access to Network Elements, WC Docket No. 04-313, Review of Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, CC Docket No. 01-338 (rel. Feb. 4, 2005) (“TRRO”).

<sup>5</sup> CompSouth notes that the Commission’s jurisdiction to set just and reasonable rates for Section 271 checklist elements is not at issue in this phase of Docket 19341-U. That issue was thoroughly addressed in the Commission’s January 20, 2006 Order Initiating Hearings. While BellSouth continues to contest the Commission’s statutory authority to address the issues herein, the Commission’s authority was not the subject of the February 20-21, 2006 hearing, and will not be addressed in CompSouth’s Post-Hearing Brief. If the Commission seeks further input on the jurisdictional issue, CompSouth is prepared to brief those issues, but does not do so here.

Gillan,<sup>6</sup> and were presented in summary form at hearing.<sup>7</sup> BellSouth's proposal for just and reasonable rates for high-capacity loops, interoffice transport and local switching was presented in the pre-filed testimony of Dr. William E. Taylor.<sup>8</sup>

The evidence at hearing showed that the parties' proposals would result in the following rates under Section 271 for the most commonly used de-listed UNEs used by CLECs in Georgia:<sup>9</sup>

De-Listed UNE	TELRIC § 251 Rate	CompSouth's Proposed §271 Rate	BellSouth's Proposed § 271 Rate
DS-1 Loops – Zone 1	\$49.41	\$85.97	\$179.15
DS-1 Transport	\$34.93	\$44.04	\$257.00
DS-3 Transport	\$349.42	\$440.53	\$2,436.00
Switching	\$4.18	\$6.86	\$11.18

CompSouth and BellSouth used extremely different methodologies to calculate their proposed Section 271 rates. CompSouth used data from BellSouth's own cost studies and prior rate proposals to establish just and reasonable rates that give BellSouth the opportunity to recover its "direct costs, plus reasonable contribution to common/overhead costs."<sup>10</sup> The prices recommended by CompSouth are "substantially above TELRIC, but are still reasonably based on direct costs plus a just and reasonable contribution to overhead."<sup>11</sup> BellSouth stakes its case on

<sup>6</sup> Tr. at 271-317, Testimony of Joseph Gillan On Behalf of The Competitive Carriers of the South, Inc. (Feb. 10, 2006) ("Gillan Direct").

<sup>7</sup> CompSouth Exhibit 5 (Gillan witness summary; includes specific rate proposals at pages 2-4).

<sup>8</sup> Tr. at 99, Direct Testimony of William E. Taylor, Ph.D. On Behalf of BellSouth Telecommunications, Inc. (Feb. 10, 2006) ("Taylor Direct"). Witnesses for BellSouth and Covad Communications, Inc. ("Covad") presented testimony specific to rates for line sharing. The line sharing rate issues are addressed in a separate post-hearing brief prepared by Covad.

<sup>9</sup> CompSouth Exhibit 5 ("TELRIC § 251 Rate" and "CompSouth's Proposed § 271 Rate" data); Tr. at 259-62 ("BellSouth's Proposed § 271 Rate" data). See Taylor Direct, at 28 and Tr. at 74 (Taylor cross-examination) (recommending Commission adopt § 271 rates consistent with BellSouth special access tariffs and "commercial" agreements); Gillan Direct at 24-32 (setting forth CompSouth's "specific just and reasonable rate proposals").

<sup>10</sup> CompSouth Exhibit 5, at 1;

<sup>11</sup> Gillan Direct, at 26.

the flawed legal position that its Section 271 rates need only reflect “what the market can bear.”<sup>12</sup> Moreover, BellSouth’s witness offered the Commission a theoretical “process” for establishing rates, but admitted he did not know what actual rates would result from his proposed process.<sup>13</sup> In fact, it was CompSouth’s witness Mr. Gillan, rather than BellSouth’s witness or counsel, who shared with the Commission the actual prices that BellSouth urges the Commission to accept as just and reasonable for de-listed UNEs. BellSouth failed to demonstrate that its proposed rates – the rates it did not even reveal in its testimony or at hearing – meet the just and reasonable standard applicable to Section 271 prices for de-listed Section 251 UNEs.

**B. CompSouth’s proposed rates are “just and reasonable” as required by Section 271.**

The standard for Section 271 rates for UNEs de-listed under Section 251 is that such rates must be “just and reasonable.” The FCC established this standard in the TRO and it was upheld by the D.C. Circuit’s decision in *USTA II*.<sup>14</sup> The FCC found that “the appropriate inquiry for network elements required only under section 271 is to assess whether they are priced on a just, reasonable and not unreasonably discriminatory basis – the standards set forth in sections 201 and 202.”<sup>15</sup> In determining how this standard should be applied, the FCC found:

Thus, the pricing of checklist network elements that do not satisfy the unbundling standards in section 251(d)(2) are reviewed utilizing the basic just, reasonable, and nondiscriminatory rate standard of sections 201 and 202 that is fundamental

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<sup>12</sup> Docket 19341-U, BellSouth Response In Opposition To CompSouth’s Emergency Motion To Compel Discovery Responses, at 3 (Feb. 6, 2006) (“[T]he test for just and reasonable is one that focuses on what the market will bear, not on a cost study.”).

<sup>13</sup> Tr. at 74 (Q: [W]hat is the intrastate special access rate that you propose is a just and reasonable rate for high capacity loops de-listed under Section 251 in Georgia? A (Taylor): Do you mean the -- the dollar value of it? Q: Yes. A (Taylor): I'm -- I don't know. I'm not familiar with the tariff.); Tr. at 75 (Q: Okay. But it's your recommendation that the Commission adopt them [tariffed special access rates], even though you don't know what they are? A (Taylor): Yes, that's correct. Q: Okay. And the answer may be similar. Just let me know if it is. What is the rate that you're proposing for dedicated interoffice transport in this proceeding? A (Taylor): Same answer.)

<sup>14</sup> See *United States Telecom Ass'n v. FCC*, 359 F.3d 554, 588-90 (D.C. Cir. 2004).

<sup>15</sup> TRO ¶ 656.

to common carrier regulation that has historically been applied under most federal and state statutes, including (for interstate services) the Communications Act. Application of the just and reasonable and nondiscriminatory pricing standard of sections 201 and 202 advances Congress's intent that Bell companies provide meaningful access to network elements.<sup>16</sup>

The FCC made clear that the just and reasonable standard is to be applied in this context as it “has historically been applied under most federal and state statutes,” and that application of the standard requires a “fact-specific inquiry”<sup>17</sup> into the proposed rates.

The FCC did not decide that any particular rates would satisfy the just and reasonable standard for purposes of Section 271. It did note that “for a given purchasing carrier, a BOC might satisfy this standard” by showing its Section 271 rate “is at or below the rate at which the BOC offers comparable functions to similarly situated purchasing carriers under its interstate access tariff, to the extent such analogues exist.”<sup>18</sup> In addition, the FCC held out the possibility that “a BOC might demonstrate that the rate at which it offers a section 271 network element is reasonable by showing that it has entered into arms-length agreements with other, similarly situated purchasing carriers to provide the element at that rate.”<sup>19</sup> These examples of how a BOC “might” meet the just and reasonable test for Section 271 rates did not, however, change the content of the test itself; rates must still meet “the basic just, reasonable, and nondiscriminatory rate standard” in order to ensure “that Bell companies provide meaningful access to network elements.”<sup>20</sup>

The FCC held in the TRO that Section 271 checklist items are not required to be offered at TELRIC-based rates.<sup>21</sup> A departure from strict adherence to the TELRIC standard, however,

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<sup>16</sup> TRO ¶ 663.

<sup>17</sup> TRO ¶ 664.

<sup>18</sup> TRO ¶ 664 (emphasis supplied).

<sup>19</sup> *Id.*

<sup>20</sup> TRO ¶ 663.

<sup>21</sup> TRO ¶ 659.

is not the same thing as abandoning regulation altogether and letting BellSouth unilaterally name its rate for Section 271 elements. In order to give meaning to the “just and reasonable” standard in the context of Section 271, the FCC tied the standard to the “historical” use of the standard under federal and state statutes. While the just and reasonable standard has evolved over the decades it has been applied by regulators, one theme has been constant: there must be a “continuing nexus between ... rates and the underlying cost of providing service.”<sup>22</sup> The necessity of this nexus between rates and underlying costs “permeates the record of FCC decisions.”<sup>23</sup> As the Supreme Court noted in reviewing the history of regulated ratemaking in its 2002 decision in *Verizon v. FCC*:

What had changed throughout the era beginning with *Smyth v. Ames* was prevailing opinion on how to calculate the most useful rate base, with disagreement between fair-value and cost advocates turning on whether invested capital was the key to the right balance between investors and ratepayers, and the price cap scheme simply being a rate-based offset to the utilities’ advantage of superior knowledge of the facts employed in cost-of-service ratemaking. What is remarkable about this evolution of just and reasonable ratesetting, however, is what did not change. The enduring feature of ratesetting from *Smyth v. Ames* to the institution of price caps was the idea that calculating a rate base and then allowing a fair rate of return on it was a sensible way to identify a range of rates that would be just and reasonable to investors and ratepayers.<sup>24</sup>

This formula, which has been consistently used for determining just and reasonable rates, provides the model used by CompSouth in formulating its just and reasonable rate proposals in this proceeding.

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<sup>22</sup> See Gillan Direct at 9, quoting Federal Communications Commission, CC Docket No. 87-313, *Report and Order and Second Further Notice of Proposed Rulemaking* (rel. April 17, 1989) at ¶ 8 (emphasis supplied).

<sup>23</sup> *Id.* at 9.

<sup>24</sup> *Verizon Comm’s v. FCC*, 535 U.S. 467, 481 (2002).

CompSouth's proposed Section 271 rates for de-listed UNEs use BellSouth's own estimate of its direct forward-looking costs, and adds to that a reasonable allocation of overhead.<sup>25</sup> The basic methodology, as summarized by Mr. Gillan at hearing is:

"Direct Cost + Reasonable Contribution to Common/Overhead Costs."<sup>26</sup>

As discussed in further detail below, the evidence demonstrated that this methodology is consistent with the "new services" standard that has been used by the FCC to establish just and reasonable rates under Section 201 and 202. The evidence showed that if the methodology is applied by the Commission as recommended by CompSouth, it will generate rates significantly higher than existing TELRIC rates. Moreover, BellSouth witnesses conceded at hearing that key components of the CompSouth methodology are indisputably correct.

Under the CompSouth proposal, the Commission would "establish just and reasonable 271 prices in this proceeding through a two step process," outlined as follows by Mr. Gillan:

\* First, for purposes of establishing Section 271 rates (and only Section 271 rates), I recommend the Commission use the forward looking prices that BellSouth proposed in Docket No. 14361-U as the direct cost for each element. The Commission has already concluded that these prices are not TELRIC compliant for, among other reasons, the fact that BellSouth's cost of capital (and other input assumptions) were inappropriate. By using these rates as an estimate of the direct cost of Section 271 prices, however, the Commission will (in effect) be (a) granting BellSouth a higher rate of return on Section 271 elements than elements offered pursuant to Section 251, and (b) the Commission will eliminate any dispute (by BellSouth) as to whether the appropriate input assumptions have been used.<sup>27</sup>

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<sup>25</sup> See Gillan Direct at 17; CompSouth Exhibit 5 at 1 (Gillan summary presentation).

<sup>26</sup> CompSouth Exhibit 5 at 1.

<sup>27</sup> BellSouth has previously claimed that its loop model reflects BellSouth's actual network routing choices and engineering rules:

The BSTLM development team recognized that a major deficiency in the existing proxy models exists in that they unsuccessfully capture the *realistic routing that occurs between points in actual telecommunications networks*. BSTLM represents the implementation of the next generation of model routing. *It combines the aspects of the MST with the knowledge of roads and the rights-of-way that the telecommunications network will typically route over*. This approach is referred to in the documentation (and in the rest of my testimony) as the Minimum Spanning Road Tree ("MSRT"). *This is a breakthrough*

\* Second, I recommend that the Commission increase the overhead loading applied to the direct cost measure described above. As the Commission is aware, TELRIC studies apply relatively low allocations of “shared and common” (or overhead) costs in developing TELRIC prices because the goal of such prices is efficient entry and competition. Although the Commission should also be concerned that entry is successful under Section 271, it would be consistent with the common application of the “just and reasonable” rate standard to permit modestly higher overhead loadings on Section 271 network elements than have traditionally been applied to Section 251 elements under TELRIC.

In addition, CompSouth proposes that non-recurring charges for Section 271 checklist items be set at the levels that would apply to Section 251 network elements.<sup>28</sup> The application of this methodology results in the proposed Section 271 rates set forth in the chart in Section II. A. above, and further detailed in Mr. Gillan’s direct testimony.<sup>29</sup>

Based on BellSouth’s own testimony in this and other proceedings, many aspects of the CompSouth just and reasonable rate proposal should not be in dispute. First, the basic overall methodology used by Mr. Gillan – known as the “new services” test<sup>30</sup> – is one recognized by BellSouth witness Dr. Taylor as a sound methodology for establishing just and reasonable rates. When asked how a regulatory body would go about establishing just and reasonable rates, Dr. Taylor identified the new services test as “the famous one” used by regulators to develop a range of just and reasonable rates.<sup>31</sup> While BellSouth apparently asserts that no ratesetting

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*approach in that it “builds” the minimum amount of plant that connects points following the road network.*

Direct Testimony of Mr. James W. Stegeman on behalf of BellSouth Telecommunications, Inc., Before the Georgia Public Service Commission, Docket No. 14361-U, October 1, 2001, pp. 23-24. Emphasis added.

<sup>28</sup> See Gillan Direct at 23-24.

<sup>29</sup> See Gillan Direct at 27 (rates for loops and associated multiplexing); 28 (interoffice transport rates); 31 (switching rates). Mr. Gillan’s recommendations are summarized in CompSouth Exhibit 5, at 2-4.

<sup>30</sup> See Tr. at 270 (Q: How does the methodology that you propose compare to what’s called the new services methodology? A (Gillan): It is basically the new services methodology. It is a direct cost, plus reasonable contribution, the common cost and overhead methodology. It’s what the FCC calls the new services test.)

<sup>31</sup> Tr. at 83 (Taylor).

methodology should be followed in this case (since it claims it can charge “what the market will bear” under Section 271), BellSouth’s own witness acknowledges that the methodology recommended by CompSouth is one that has a long and credible history in telecommunications regulation.

Second, BellSouth does not dispute that the appropriate measure of costs is “forward-looking” costs (as opposed to BellSouth’s “embedded” or “historical” costs). Mr. Gillan documents in his testimony that, as the just and reasonable standard evolved, the FCC came to favor use of prospective, *i.e.*, forward-looking costs as the basis for setting rates.<sup>32</sup> BellSouth witness Dr. Taylor agrees: “[T]he FCC has accepted the premise that rates *based on* forward-looking cost measures (not necessarily TELRIC but others as well) are superior to historical or embedded costs for setting just and reasonable rates, particularly so in competitive markets.”<sup>33</sup> Thus, there should be no dispute about CompSouth’s use of BellSouth’s estimate of its forward-looking costs. Moreover, since CompSouth’s analysis used BellSouth’s own *proposed* estimates of its direct forward-looking costs (as opposed to the costs approved by the Commission), BellSouth should not be heard to complain that the costs are not appropriate for its network. CompSouth’s use of BellSouth’s own forward-looking cost data serves to, if anything, over-compensate BellSouth for its provision of de-listed UNEs under Section 271.<sup>34</sup>

Third, BellSouth agrees that the rates proposed in its filed TELRIC studies (the ones used by CompSouth in developing its just and reasonable rate recommendation) “fully recover its

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<sup>32</sup> See Gillan Direct at 13-14.

<sup>33</sup> Taylor Direct at 6 (emphasis in original).

<sup>34</sup> See Tr. at 186 (Gillan) (“[T]hat very step of using their filed TELRIC [in CompSouth’s methodology] not only gives them more money, higher prices than the Commission later found was appropriate for TELRIC, but if you look at some of the trade secret documents that were distributed, you’ll see that these filed TELRIC rates are themselves substantially above BellSouth’s incremental cost, at least for switching . . . .”)

costs in a forward looking model.”<sup>35</sup> In describing how BellSouth arrived at its Section 271 switching rate, BellSouth witness Ms. Tipton stated that BellSouth looked at its “filed TELRIC rate that BellSouth believes fully recovers its costs in a forward looking model.”<sup>36</sup> BellSouth thus cannot contest that its filed TELRIC study rate used to develop CompSouth’s just and reasonable rates fully recover BellSouth’s costs. This makes sense: the studies were submitted by and supported by BellSouth, so one would expect BellSouth to have included all its direct forward-looking costs into such rates. While CompSouth does not concede that these rates accurately reflect BellSouth’s actual TELRIC costs, there can be no question that they adequately cover all BellSouth’s direct costs for purposes of establishing Section 271 just and reasonable rates.

Fourth, BellSouth has filed testimony in previous rate proceedings acknowledging that its concerns about TELRIC rates being compensatory do not apply to switching and interoffice transport (but rather primarily to unbundled loops). BellSouth sponsored testimony in a South Carolina proceeding in which its witness testified that BellSouth’s concerns with the FCC’s TELRIC methodology do not apply to switching and transport network elements:

... it is the additional constraints currently mandated by the FCC that the incumbent local exchange carriers (“ILECs”) object to with respect to TELRIC-based rates. The use of a hypothetical network and most efficient, least-cost provider requirements have distorted the TELRIC results and normally understate the true forward-looking costs of the ILEC.

These distortions, however, are most evident in the calculation of unbundled loop elements, and they are less evident in the switching and transport network elements that make up switched access. In fact, if BellSouth had conducted a TSLRIC study for switched access, the underlying assumptions with respect to

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<sup>35</sup> Tr. at 162 (Tipton).

<sup>36</sup> *Id.*

forward-looking equipment and architectures would have been consistent with those used in the TELRIC studies for switching and transport UNEs.<sup>37</sup>

Moreover, BellSouth has explained in previous filings that a rate is compensatory if it covers its Total Service LRIC (“TSLRIC”), which is less than TELRIC.<sup>38</sup> Thus, a TELRIC-based rate covers its costs and provides contribution to shared and common costs as well:

Since TSLRIC reflects all of the direct costs ... TSLRIC studies are the basis of testing for cross-subsidization. If rates for a service exceed the service’s TSLRIC ..., then the service is not being subsidized by other services.<sup>39</sup>

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... all else being held constant, the allowance of shared and common costs under the TELRIC cost methodology increases costs above those that would have been obtained from a comparable TSLRIC switched access study.<sup>40</sup>

As the above explains, using TELRIC – particularly BellSouth’s filed TELRIC studies – to estimate the direct cost of an element should be relatively non-controversial. Properly implemented, the method computes an average total cost that fully compensates BellSouth for the forward looking costs of providing network facilities. Moreover, as Mr. Gillan testified, for transport and switching, “FCC rules do not optimize the network, but instead require that actual wire center locations and generally model technologies – fiber and digital switching – that have

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<sup>37</sup> Testimony of Robert McKnight on behalf of BellSouth, Public Service Commission of South Carolina, Docket No. 1997-239-C at 7-8 (Dec. 31, 2003) (emphasis supplied) (“McKnight Testimony”). Pursuant to Staff’s request at hearing, CompSouth is filing a copy of the McKnight testimony in this docket.

<sup>38</sup> The FCC has recognized that the TSLRIC methodology is an acceptable method to establish direct costs:

TELRIC is the specific forward-looking methodology described in 47 C.F.R. § 51.505 and required by our rules for use by states in determining UNE prices. States often use “total service long run incremental cost” (TSLRIC) methodology in setting rates for intrastate services. It is consistent with the *Local Competition Order* for a state to use its accustomed TSLRIC methodology (or another forward-looking methodology) to develop the direct costs of payphone line service costs.

*Payphone Order*, ¶ 49 (footnotes omitted) quoted in Gillan Direct at 20.

<sup>39</sup> McKnight Testimony at 6.

<sup>40</sup> McKnight Testimony, at 8.

actually been implemented in the network.”<sup>41</sup> Consequently, BellSouth has no basis to contest that TELRIC-based estimates of direct costs are an appropriate starting point to establish Section 271 prices.

Fifth, BellSouth has no basis to contest CompSouth’s switching rate of TELRIC plus \$2.78.<sup>42</sup> BellSouth’s “standard” rate under the commercial agreements is much higher, at TELRIC plus \$7.00. Cross-examination regarding BellSouth’s “commercial agreements,” however, revealed that one CLEC received a rate for switching lower than the CompSouth proposal.<sup>43</sup> BellSouth’s witness claimed that the dramatically lower rate was justified by unspecified “volume and term discounts.”<sup>44</sup> BellSouth presented no evidence, however, showing that switching is usage sensitive, *i.e.*, that switching volumes would provide a rational basis for discounting the switching rate offered. Moreover, the data presented by Mr. Gillan regarding the efficacy of a flat (as opposed to usage sensitive) switching rate structure demonstrates there is no cost basis for such a volume or term discount.<sup>45</sup> With no basis for such a discount, it is difficult to understand why BellSouth would negotiate such a rate with one CLEC but oppose a similar rate as not compliant with the just and reasonable standard.

As to the issues listed above, the evidence shows that BellSouth’s own testimony demonstrates either agreement with the CompSouth methodology or eliminates any rationale

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<sup>41</sup> Gillan Direct at 20-21.

<sup>42</sup> Tr. at 261 (Mr. Gillan identifying the CompSouth switching rate on a “TELRIC plus” basis).

<sup>43</sup> See Tr. at 262 (Gillan) ([T]here’s one carrier, carrier 12 that is if -- if that chart is accurate and it’s BellSouth’s chart and their witness testified yesterday that it’s accurate, our proposal in this docket is significantly higher than the rate that they voluntarily have provided to carrier 12.”) The “chart” to which Mr. Gillan is referring is confidential CompSouth Exhibit 1, BellSouth’s spreadsheet entitled “Signed Commercial Agreements Georgia Only Information.” The CLEC that negotiated the lower rate referenced here and at hearing is identified on CompSouth Exhibit 1 as “carrier 12” or “CLEC 12.” To protect the BellSouth’s assertion of confidentiality, CompSouth will not identify the CLEC or the particular rate in this Brief.

<sup>44</sup> Tr. at 160-62 (Tipton).

<sup>45</sup> See Gillan Direct at 28-30.